

OTTUMWA WATER WORKS
OTTUMWA, IOWA

INDEPENDENT AUDITOR'S REPORT
BASIC FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION
SCHEDULE OF FINDINGS

DECEMBER 31, 2011

OTTUMWA WATER WORKS

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OTTUMWA WATER WORKS

OFFICIALS
DECEMBER 31, 2011

<u>NAME</u>	<u>TITLE</u>	<u>TERM EXPIRES</u>
Jack Kirk	Water Works Trustee	July, 2012
Teri Messerschmitt	Water Works Trustee	July, 2013
Pete Rich	Water Works Trustee	July, 2014
Clive Parcell	Water Works Trustee	July, 2015
Barb Allison	Water Works Trustee	July, 2016
Michael Heffernan	General Manager	Indefinite

INDEPENDENT AUDITOR'S REPORT

Board of Trustees
Ottumwa Water Works
Ottumwa, Iowa

We have audited the accompanying financial statements of Ottumwa Water Works as of and for the year ended December 31, 2011 as listed in the table of contents. These financial statements are the responsibility of Ottumwa Water Works' management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Ottumwa Water Works as of December 31, 2011, and the changes in it's financial position and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated September 25, 2012 on our consideration of the Utility's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

Management's Discussion and Analysis, Budgetary Comparison Information and the Schedule of Funding Progress for the Retiree Health Plan on pages 4 through 6 and 19 through 20 are not required parts of the basic financial statements, but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. We did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Utility's financial statements as a whole. Other supplementary information is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in our audit of the financial statements and in our opinion is fairly stated in all material respects in relation to the financial statements as a whole.

ANDERSON, LARKIN & CO. P.C.

Ottumwa, Iowa
September 25, 2012

MANAGEMENT'S DISCUSSION AND ANALYSIS

Ottumwa Water Works provides this Management's Discussion and Analysis of its financial statements. This narrative overview and analysis of the financial activities is for the calendar year ended December 31, 2011. We encourage readers to consider this information in conjunction with the Utility's financial statements which follow.

FINANCIAL HIGHLIGHTS

The Utility's operating revenues increased by approximately 8.0% or \$431,612 from 2010 to 2011. Increases in revenue from the sale of water accounted for the majority of the increase.

The Utility's operating expenses increased approximately 6.9% or \$350,372 from 2010 to 2011. This increase included an increase in production and distribution expenses and a decrease in general plant expenses.

The Utility's net assets increased approximately 5.8% or \$1,308,721 from 2010 to 2011.

USING THIS ANNUAL REPORT

The Ottumwa Water Works is a publicly owned utility and presents its financial statements using the economic resources measurement focus and the accrual basis of accounting which is the same measurement focus and basis of accounting employed by private sector business enterprises. This discussion and analysis is intended to serve as an introduction to Ottumwa Water Work's basic financial statements. The annual report consists of a series of financial statements and other information as follows:

Management's Discussion and Analysis introduces the basic financial statements and provides an analytical overview of the Utility's financial activities.

The Statement of Net Assets presents information about the Utility's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Utility is improving or deteriorating.

The Statement of Revenues, Expenses and Changes in Net Assets is the basic statement of activities for proprietary funds. This statement presents information on the Utility's operating revenues and expenses, non-operating revenues and expenses and whether the Utility's financial position has improved or deteriorated as a result of the year's activities.

The Statement of Cash Flows presents the change in the Utility's cash and cash equivalents during the year. This information can assist the user of the report in determining how the Utility financed its activities and how it met its cash requirements.

The Notes to Financial Statements provide additional information essential to a full understanding of the data provided in the basic financial statements.

Required Supplementary Information further explains and supports the financial statements with a comparison of the City's budget for the year, as well as presenting the Schedule of Funding Progress for the Retiree Health Plan.

FINANCIAL ANALYSIS OF THE UTILITY

Statement of Net Assets

As noted earlier, net assets may serve over time as a useful indicator of the Utility's financial position. The Utility's net assets as of December 31, 2011 total \$23,939,326. This compares to \$22,630,605 as of December 31, 2010. A summary of the Utility's net assets as of December 31, 2011 and 2010 are presented below.

NET ASSETS

	December 31,	
	<u>2011</u>	<u>2010</u>
Current assets	\$ 7,453,422	\$ 7,609,873
Capital assets at cost, less accumulated depreciation	27,558,846	25,341,832
Other assets	113,772	88,112
Total assets	<u>35,126,040</u>	<u>33,039,817</u>
Current liabilities	2,953,394	2,574,531
Long-term liabilities	8,233,320	7,834,681
Total liabilities	<u>11,186,714</u>	<u>10,409,212</u>
Unrestricted assets	5,082,026	5,515,169
Invested in capital assets, net of related debt	18,857,300	17,115,436
Total net assets	<u>\$ 23,939,326</u>	<u>\$ 22,630,605</u>

Statements of Revenues, Expenses and Changes in Net Assets

Operating revenues are received from the sale of water to Ottumwa residents, sale of hydro electric power, and other miscellaneous income. Non-operating revenues and expenses include interest income and interest expense. The utilization of capital assets is reflected in the financial statements as depreciation, which allocates the cost of an asset over its expected useful life. A summary of revenues, expenses and changes in net assets for the years ended December 31, 2011 and 2010 is presented below:

CHANGES IN NET ASSETS

	Year Ended December 31,	
	<u>2011</u>	<u>2010</u>
Operating revenue:		
Sale of water	\$ 4,887,878	\$ 4,381,217
Sale of electricity	492,983	571,951
Miscellaneous income	425,395	421,476
Total operating revenue	<u>5,806,256</u>	<u>5,374,644</u>
Operating expenses:		
Production	1,239,906	1,070,759
Distribution	1,464,958	1,110,034
Hydro	218,312	197,737
Financial services	304,201	282,236
Administration	285,921	354,771
General plant	760,550	872,561
Depreciation and amortization	1,143,170	1,178,548
Total operating expenses	<u>5,417,018</u>	<u>5,066,646</u>
Operating income	389,238	307,998
Nonoperating revenue (expense):		
Interest income	84,144	92,421
Grant proceeds	565,830	-
Forgivable loan proceeds	560,000	-
Interest expense	(290,491)	(276,944)
Total nonoperating revenue (expense)	<u>919,483</u>	<u>(184,523)</u>
Change in net assets	1,308,721	123,475
Net assets – Beginning of year	<u>22,630,605</u>	<u>22,507,130</u>
Net assets – End of year	<u>\$ 23,939,326</u>	<u>\$ 22,630,605</u>

The Statement of Revenues, Expenses and Changes in Net Assets reflects an increase in the net assets at the end of the year.

During calendar year 2011, operating revenues increased 8.0%, or \$431,612. Water revenue increased \$506,661 due to higher sales volume. Electricity revenue decreased \$78,968 or 13.8% due to river levels affecting when electricity was able to be produced. Employee benefits that were previously classified under administration and general plant have been allocated to all divisions based upon payroll by division. This resulted in increases in production, distribution, hydro and financial services expenses, and is offset by decreases in administration and general plant expenses.

Statement of Cash Flows

The Statement of Cash Flows presents information related to cash inflows and outflows, summarized by operating, capital and related financing activities and investing activities. Cash flows from operating activities include the sale of water, electricity and other receipts reduced for payments to suppliers and employees. Cash flows from capital and related financing activities include the purchase of capital assets. Cash flows from investing activities include interest income and the purchase and redemption of certificates of deposit. Cash flows from financing activities include proceeds and payments related to the Utility's debt.

Budget

The Utility submits a budget to the City of Ottumwa on an annual basis. Receipts for the year exceeded the amounts budgeted by \$1,497,347 and disbursements were less than amounts budgeted by \$674,614. The increase in receipts was a result of grants and the forgivable loan received.

CAPITAL ASSETS

At December 31, 2011, the Utility had \$27,558,846, invested in capital assets, net of accumulated depreciation of \$23,893,084. Depreciation and amortization charges totaled \$1,143,170 for the year. More detailed information about the Utility's capital assets is presented in the Notes to Financial Statements.

LONG-TERM DEBT

At December 31, 2011, the Utility had \$8,753,850 in total long-term debt outstanding. During the year ended December 31, 2011, the Utility issued a total of \$902,743 of long-term debt to finance Utility construction projects. Additional information regarding the Utility's long-term debt is included in the Notes to Financial Statements.

ECONOMIC FACTORS

During 2011, Ottumwa Waters Works' financial position increased. The current condition of the economy in the State continues to be a concern for Utility officials. Some of the realities that may potentially become challenges for the Utility to meet are:

The Utilities distribution system requires constant maintenance and upkeep.

The continued inflationary increases in health care, chemicals, and energy costs.

Technology continues to expand and current technology becomes outdated presenting an on-going challenge to maintain up to date technology at a reasonable cost.

The Utility anticipates the current year will be much like the last and we will maintain a close watch over resources to maintain our ability to react to unknown issues.

CONTACTING THE UTILITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, customers and creditors with a general overview of the Utility's finances and to show the Utility's accountability for the money it receives. If you have questions about this report or need additional financial information, contact Ottumwa Water Works, P.O. Box 20, Ottumwa, Iowa.

OTTUMWA WATER WORKSSTATEMENT OF NET ASSETS
DECEMBER 31, 2011ASSETSCURRENT ASSETS:

Cash and cash equivalents	\$ 2,073,453
Certificates of deposit	3,690,000
Accounts receivable, net of allowance for uncollectible accounts	1,451,994
Inventory	210,964
Accrued interest receivable	2,049
Prepaid expenses	24,962
Total current assets	<u>7,453,422</u>

CAPITAL ASSETS:

Buildings	6,305,772
Water distribution system	41,717,195
Equipment and vehicles	1,936,688
Office equipment	663,592
Total	<u>50,623,247</u>
Less accumulated depreciation	<u>23,893,084</u>
Depreciated value of capital assets	26,730,163
Land	618,577
Construction in progress	210,106
Total capital assets	<u>27,558,846</u>

OTHER ASSETS:

Deferred charges - Debt issue costs	<u>113,772</u>
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TOTAL ASSETS	<u>35,126,040</u>
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CURRENT LIABILITIES:

Accounts payable	553,525
Accrued payroll and related expenses	38,410
Accrued interest	37,939
Sales tax	16,730
Sick leave	202,709
Accrued vacation	76,312
Self insurance	42,445
Accrued disability and life insurance	132,207
Customer deposits	233,151
Current maturities of long-term liabilities	520,530
Accrued sewer and refuse collections	1,099,436
Total current liabilities	<u>2,953,394</u>

<u>LONG-TERM LIABILITIES</u> - Less current maturities	<u>8,233,320</u>
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TOTAL LIABILITIES	<u>11,186,714</u>
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NET ASSETS:

Unrestricted	5,082,026
Invested in capital assets, net of related debt	<u>18,857,300</u>

TOTAL NET ASSETS	\$ <u>23,939,326</u>
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See Accompanying Notes to the Financial Statements

OTTUMWA WATER WORKS

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
YEAR ENDED DECEMBER 31, 2011

OPERATING REVENUE:

Sale of water	\$ 4,887,878
Sale of electricity	492,983
Miscellaneous income	425,395
Total operating revenue	<u>5,806,256</u>

OPERATING EXPENSES:

Production	1,239,906
Distribution	1,464,958
Hydro	218,312
Financial services	304,201
Administration	285,921
General plant	760,550
Depreciation and amortization	<u>1,143,170</u>
Total operating expenses	<u>5,417,018</u>

OPERATING INCOME 389,238

NONOPERATING REVENUE (EXPENSE):

Grant proceeds	565,830
Forgivable loan proceeds	560,000
Interest income	84,144
Interest expense	<u>(290,491)</u>
Total nonoperating revenue (expense)	<u>919,483</u>

CHANGE IN NET ASSETS 1,308,721

NET ASSETS - BEGINNING OF YEAR 22,630,605

NET ASSETS - END OF YEAR \$ 23,939,326

OTTUMWA WATER WORKS

STATEMENT OF CASH FLOWS
YEAR ENDED DECEMBER 31, 2011CASH FLOWS FROM OPERATING ACTIVITIES:

Cash received from customers	\$ 5,464,415
Cash received from other operating receipts	425,395
Cash paid to suppliers for goods and services	(2,818,598)
Cash paid to employees for services	(1,382,088)
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>1,689,124</u>

CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:

Purchase of capital assets	<u>(3,355,184)</u>
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CASH FLOWS FROM INVESTING ACTIVITIES:

Interest on investments	83,898
Purchase of certificates of deposit	(1,500,000)
Proceeds from certificates of deposit	2,000,000
NET CASH PROVIDED BY INVESTING ACTIVITIES	<u>583,898</u>

CASH FLOWS FROM FINANCING ACTIVITIES:

Proceeds from long-term debt	872,083
Principal payments on long-term debt	(427,593)
Payment of interest on long-term debt	(290,491)
Proceeds from forgivable debt	560,000
Proceeds from grants	565,830
NET CASH PROVIDED BY FINANCING ACTIVITIES	<u>1,279,829</u>

NET INCREASE IN CASH AND CASH EQUIVALENTS 197,667

CASH AND CASH EQUIVALENTS - Beginning of year 1,875,786

CASH AND CASH EQUIVALENTS - End of year \$ 2,073,453

RECONCILIATION OF OPERATING INCOME TO NET CASHPROVIDED BY OPERATING ACTIVITIES:

Operating income	\$ 389,238
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation and amortization expense	1,143,170
Increase in allowance account	16,500
Change in operating assets and liabilities:	
Increase in accounts receivable	(87,053)
Increase in inventory	(75,970)
Decrease in prepaid expenses	887
Increase in accounts payable	78,735
Increase in accrued payroll and related expenses	9,681
Increase in accrued interest	3,839
Increase in sales tax	3,315
Increase in sick leave	15,377
Increase in accrued vacation	5,018
Increase in self insurance	26,169
Increase in accrued disability and life insurance	14,067
Increase in customer deposits	14,146
Increase in accrued sewer and refuse collections	122,579
Increase in net OPEB obligation	9,426
NET CASH PROVIDED BY OPERATING ACTIVITIES	\$ <u>1,689,124</u>

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:

Cash paid for interest	\$ <u>286,652</u>
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See Accompanying Notes to the Financial Statements

OTTUMWA WATER WORKS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Ottumwa Water Works is organized as a municipal water utility which was established in 1910. They are overseen by a five member board appointed by the City Council and Mayor of the City of Ottumwa. The Utility's operating budget is subject to the approval of the City Council. The Water Works is considered by the City of Ottumwa to be substantially autonomous. The Water Works is funded entirely by water user charges collected from users of the Water Works' system.

The financial statements of the Water Works are prepared in conformity with U.S. generally accepted accounting principles (GAAP) as prescribed by the Governmental Accounting Standards Board.

Reporting Entity

For financial reporting purposes, Ottumwa Water Works has included all funds, organizations, agencies, boards, commissions and authorities. The Utility has also considered all potential component units for which it is financially accountable and other organizations for which the nature and significance of their relationship with the Utility are such that exclusion would cause the Utility's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Utility to impose its will on that organization or (2) the potential for the organization to provide specific benefits to or impose specific financial burdens on the Utility. Ottumwa Water Works has no component units which meet the Governmental Accounting Standards Board criteria.

Ottumwa Water Works is not presented as a Component Unit in the City of Ottumwa's financial statements. The Utility is a legally separate entity from the City, but is financially accountable to the City. The Utility is governed by a five-member Board appointed by the City Council and the Utility's operating budget is subject to the approval of the City Council.

Basis of Presentation

The accounts of the Ottumwa Water Works are organized as an enterprise fund. Enterprise funds are used to account for operations (a) financed and operated in a manner similar to private business enterprises, where the intent of the governing body is the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges or (b) where the governing body has decided periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability or other purposes.

Measurement Focus and Basis of Accounting

The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

The Ottumwa Water Works applies all applicable GASB pronouncements, as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements; Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedure.

The Ottumwa Water Works distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Utility's principal ongoing operations. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

OTTUMWA WATER WORKS

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2011

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Assets, Liabilities and Net Assets

The following accounting policies are followed in preparing the Statement of Net Assets:

Cash, Investments and Cash Equivalents – The Ottumwa Water Works considers all short-term investments that are highly liquid to be cash equivalents. Cash equivalents are readily convertible to known amounts of cash and, at the day of purchase, have a maturity date no longer than three months. Cash investments not meeting the definition of cash equivalents at December 31, 2011 include certificates of deposit of \$3,690,000.

Accounts Receivable – Ottumwa Water Works grants credit to customers, substantially all of whom are located in Ottumwa, Iowa. The risk of loss on the accounts receivable is the balance due at the time of default. Accounts receivable are considered past due after 30 days and are charged off when management determines the account is uncollectible. The Ottumwa Water Works uses the reserve method of accounting for uncollectible accounts. At December 31, 2011, a reserve of \$148,843 is provided to allow for uncollectible customer accounts.

Material and Chemicals Inventory – Inventories are stated at the lower of cost (determined on a first-in, first-out basis) or market.

During 1992, the Ottumwa Water Works changed its purchased material goods inventory to carry only selected groups of items and material individual items over a predetermined dollar amount. All other small parts and immaterial cost items will be expensed when purchased.

Capital Assets – Capital assets are accounted for at historical cost. Depreciation of all exhaustible capital assets is charged as an expense against operations. The cost of repair and maintenance is charged to expense, while the cost of renewals or substantial betterments is capitalized. The cost and accumulated depreciation of assets disposed of are deleted, with any gain or loss recorded in current operations.

Reportable capital assets are defined by the Utility as assets with initial, individual costs in excess of the following thresholds and estimated useful lives in excess of one year.

<u>Asset Class</u>	<u>Amount</u>
Buildings	\$ 500
Water distribution system	500
Equipment and vehicles	500
Office equipment	500
Intangible assets	500

Capital assets of the Utility are depreciated using the straight line method over the following estimated useful lives:

<u>Asset Class</u>	<u>Estimated Useful lives (In years)</u>
Buildings	15-25
Water distribution system	40-50
Equipment and vehicles	5-7
Office equipment	5-7
Intangible assets	5-7

Interest is capitalized on qualified assets acquired with certain tax-exempt debt. The amount of interest to be capitalized is calculated by offsetting interest expense incurred from the date of the borrowing until completion of the project with interest earned on invested proceeds over the same period. There were no qualifying assets acquired during the year ended December 31, 2011.

OTTUMWA WATER WORKS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Compensated Absences – Utility employees accumulate a limited amount of earned but unused vacation hours for subsequent use or for payment upon termination, death or retirement. The Utility's liability for accrued vacation has been computed based on rates of pay in effect at December 31, 2011.

Use of Estimates – Management uses estimates and assumptions in preparing financial statements. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. Accordingly, actual results could differ from those estimates.

Budgets and Budgetary Accounting – The Budgetary comparison and related disclosures are reported as Required Supplementary Information. During the year ended December 31, 2011, disbursements did not exceed the amounts budgeted.

NOTE 2 – CASH AND INVESTMENTS

The Utility's deposits in banks at December 31, 2011 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The Municipal Utility is authorized by statute to invest public funds in obligations of the United States government, its agencies and instrumentalities; certificates of deposit or other evidences of deposit at federally insured depository institutions approved by the Utility Board of Trustees; prime eligible bankers acceptances; certain high rated commercial paper; perfected repurchase agreements; certain registered open-end management investment companies; certain joint investment trusts; and warrants or improvement certificates of a drainage district.

The Utility had no investments meeting the disclosure requirements of Governmental Accounting Standards Board Statement No. 3, as amended by Statement No. 40.

NOTE 3 – CAPITAL ASSETS

A summary of capital assets at December 31, 2011 is as follows:

	Balance December 31, 2010	Additions/ Reclassifications	Deletions/ Reclassifications	Balance December 31, 2011
Capital assets, being depreciated/amortized:				
Buildings	\$ 6,258,172	\$ 47,600	\$ -	\$ 6,305,772
Water distribution system	38,362,342	3,354,853	-	41,717,195
Equipment and vehicles	1,923,909	12,779	-	1,936,688
Office equipment	661,912	1,680	-	663,592
Total capital assets, being depreciated/amortized	47,206,335	3,416,912	-	50,623,247
Less accumulated depreciation/amortization	22,754,914	1,138,170	-	23,893,084
Total capital assets being depreciated/amortized, net	24,451,421	2,278,742	-	26,730,163
Capital assets, not being depreciated/amortized:				
Land	618,577	-	-	618,577
Construction in progress	271,834	3,340,725	3,402,453	210,106
Capital assets, net	\$ 25,341,832	\$ 5,619,467	\$ 3,402,453	\$ 27,558,846

OTTUMWA WATER WORKS

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2011

NOTE 4 – PENSION AND RETIREMENT BENEFITS

The Utility contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits established by state statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, P.O. Box 9117, Des Moines, Iowa, 50306-9117.

Plan members are required to contribute 5.38% and 4.50% of their annual covered salary and the Utility is required to contribute 8.07% and 6.95% of annual covered payroll for the years ended June 30, 2012 and 2011, respectively. Contribution requirements are established by state statute. The Utility's contributions to IPERS for the years ended December 31, 2011, 2010 and 2009 were \$101,850, \$91,180, and \$77,318, respectively, equal to the required contributions for each year.

NOTE 5 – SELF INSURANCE PROGRAM

The Utility has a self-insurance program for hospitalization and medical coverage for its employees. The program is administered through a service agreement with Cottingham Butler. The Utility limits its losses through the use of stop-loss policies from reinsurers. Specific individual losses for claims are limited to \$20,000 a year. The Utility's aggregate annual loss limitation is based on a formula that considers, among other things, the total number of employees. For December 31, 2011, the Utility incurred \$475,425 in expense under the program.

Amounts payable by Ottumwa Water Works at December 31, 2011 total \$42,455 which is for incurred but not reported (IBNR) and reported but not paid claims. The amounts are based on estimates of the amounts necessary to pay prior-year and current-year claims. A liability has been established based on the requirements of Governmental Accounting Standards Board Statement Number 10, which requires that a liability for claims be reported if information prior to the issuance of the financial statements indicates that it is probable that a liability has been incurred at the date of the financial statements and the amount of the loss can be reasonably estimated. Settlements have not exceeded the stop-loss coverage in any of the past three years. A reconciliation of changes in the aggregate liability for claims for the current year is as follows:

Unpaid claims as of December 31, 2010	\$ 16,276
Incurred claims (including claims incurred but not reported as of December 31, 2011):	
Provision for current-year events where the Utility has retained risk of loss	475,425
Payments:	
Claims attributable to current-year events where the Utility has retained risk of loss	449,246
Unpaid claims as of December 31, 2011	\$ 42,455

NOTE 6 – OTHER EMPLOYEE BENEFITS

The Water Works employees accumulate sick leave and vacation hours for subsequent use. The liability for accrued vacation at December 31, 2011 is \$76,312. The Water Works has a policy of paying one-half of the unused accumulated sick leave upon retirement of any employee. The maximum number of days an employee can accumulate is 120. Upon the death of any employee, 100% of the accumulated sick leave is paid. One-half of unused sick leave totals \$202,709, and is reflected in the financial statements as a liability at December 31, 2011.

OTTUMWA WATER WORKS

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2011

NOTE 6 – OTHER EMPLOYEE BENEFITS (Continued)

Effective November 1, 1989, the Water Works began a long-term disability plan. Once an employee has accumulated the maximum number of days of sick leave referred to in the preceding paragraph, they begin to accumulate long-term disability days. The days are accumulated at 50% of the normal sick leave accrual rate, and the maximum number of days to be accrued is 120. The compensation is computed at 60% of the employee's normal salary and is paid only after all normal sick leave benefits are exhausted.

The amount of the accrual reflected on the balance sheet at December 31, 2011 for the long-term disability benefit is \$127,207.

NOTE 7 – POST RETIREMENT BENEFITS

On July 22, 1992, the Ottumwa Water Works approved a policy to drop the group term life insurance coverage on existing retirees and instead pay a one-time death benefit equal to the term coverage in effect as of this date. The total death benefit payable as of December 31, 2011 was \$5,000 and covers five retirees. Only these five retirees are covered by this provision. Any other employees retiring on or after July 22, 1992 will not receive this benefit.

NOTE 8 – DESIGNATED ASSETS

The Ottumwa Water Works has designated assets comprised of demand deposits, passbook savings, and certificates of deposits that are to be used for a specific purpose. A summary of the designated assets is as follows:

Meter Deposit Fund – This fund is used to account for cash collected on customer deposits. The amount designated for the meter deposit fund as of December 31, 2011 is \$190,000.

NOTE 9 – RELATED PARTY TRANSACTIONS

The Water Works provides billing and collection services to the City of Ottumwa for sewer and refuse services. The following is a summary of the balances due to the City at December 31, 2011:

Accrued sewer services charges	\$ 821,482
Accrued refuse collection fees	<u>277,954</u>
Total accrued sewer and refuse collections	\$ <u>1,099,436</u>

NOTE 10 – LONG-TERM LIABILITIES

A summary of the changes in long-term liabilities for the year ended December 31, 2011, is as follows:

	Balance Beginning Of Year	Increases	Decreases	Balance End Of Year	Due Within One Year
Revenue Bonds	\$ 7,436,000	\$ 902,743	\$ 368,000	\$ 7,970,743	\$ 459,000
Contract Payable	790,396	-	59,593	730,803	61,530
Net OPEB Liability	42,878	9,426	-	52,304	-
Total	\$ <u>8,269,274</u>	\$ <u>912,169</u>	\$ <u>427,593</u>	\$ <u>8,753,850</u>	\$ <u>520,530</u>

OTTUMWA WATER WORKS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011

NOTE 10 – LONG-TERM LIABILITIES (Continued)

The resolutions providing for the issuance of the fully matured revenue bonds include the following provisions:

- (a) The bonds will only be redeemed from the future earnings of the enterprise activity and the bond holders hold a lien on the future earnings of the funds.
- (b) Sufficient monthly cash transfers shall be made to a water revenue bond sinking account for the purpose of making bond principal and interest payments when due.
- (c) Additional monthly cash transfers shall be made to a bond and interest reserve account until there has been accumulated an amount equal to two years' interest on the bonds then outstanding. This account is restricted for the purpose of paying bond principal and interest should funds be insufficient in the water revenue bond sinking account.
- (d) In addition, there shall be deposited to a capital improvement and extension account the sum of \$3,000 each month until there has been accumulated a sum of \$500,000. This account shall be used solely and only to pay bonds and interest should deficiencies exist in the water revenue bond sinking account or the bond and interest reserve account to pay subordinate revenue bonds issued to make necessary improvements and extensions to pay for capital improvements and extensions to the existing Water Works' plan not covered by issuance of bonds and to call and redeem such bonds as they may be then subject to redemption prior to maturity.
- (e) There shall also be paid into a bond redemption account on a monthly basis one-half of the balance of net earnings remaining after first making the required payments into the water revenue bond sinking account, the bond and interest reserve account and the capital improvement and extension account. This account is restricted to remedying any deficiency in the other required accounts. The Water Works reserves, in the aforementioned accounts, exceed the outstanding bond and interest amounts and therefore, this provision does not apply.

Contract Payable to City of Ottumwa, Iowa

During 2006 and 2010, the Water Works entered into agreements with the City of Ottumwa, Iowa, which are related to the City's sewer separation project. In the agreements, the Water Works agrees to reimburse the City for the cost of the project that relates to water main replacement. The City of Ottumwa, Iowa has paid for the entire cost of the project by issuing revenue bonds and the Water Works will pay the City of Ottumwa, Iowa for its portion of the project. Phase I requires twenty annual installments of \$39,216 starting June 1, 2008. Phase II requires eight annual installments of \$46,065 starting June 1, 2010. Both agreements include interest at 3.25%.

Iowa Department of Natural Resources

On June 2, 2005, the Utility entered into agreements with the Iowa Department of Natural Resources and Wells Fargo Bank Iowa, N.A. for the issuance of \$4,000,000 of water revenue bonds, with an interest rate of 3.0% per annum. The bonds were issued pursuant to the provisions of Chapter 384 and Section 384.24A of the Code of Iowa to pay the costs of constructing improvements and extensions to the water system.

On December 28, 2006, the Utility entered into agreements with the Iowa Department of Natural Resources and Wells Fargo Bank Iowa, N.A. for the issuance of \$4,800,000 of water revenue bonds, with an interest rate of 3.0% per annum. The bonds were issued pursuant to the provisions of Chapter 384 and Section 384.24A of the Code of Iowa to pay the costs of constructing improvements and extensions to the water system.

OTTUMWA WATER WORKS

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2011

NOTE 10 – LONG-TERM DEBT (Continued)

Iowa Department of Natural Resources(Continued)

On September 7, 2011, the Utility entered into agreements with the Iowa Department of Natural Resources and the Iowa Finance Authority for the issuance of \$1,666,000 of water revenue bonds, with an interest rate of 3.0% per annum. The loans also require the Utility to annually pay a .25% servicing fee on the outstanding principal balance. The bonds were issued pursuant to the provisions of Chapter 384 and Section 384.24A of the Code of Iowa to pay the costs of constructing improvements and extensions to the water system. During the year ended December 31, 2011, \$62,743 was drawn down on the loan.

On March 31, 2011, the Utility entered into agreements with the Iowa Department of Natural Resources and the Iowa Finance Authority for the issuance of \$1,400,000 of water revenue bonds, with an interest rate of 3.0% per annum. The loans also require the Utility to annually pay a .25% servicing fee on the outstanding principal balance. The bonds were issued pursuant to the provisions of Chapter 384 and Section 384.24A of the Code of Iowa to pay the costs of constructing improvements and extensions to the water system. During the year ended December 31, 2011, \$1,400,000 was drawn down on the loan. During the year ended December 31, 2011, the Utility paid interest of \$21,541 on this loan. Included in the \$1,400,000 loan is a provision for forgivable water revenue bonds. The bonds were issued pursuant to the provisions of Chapter 384.24A of the Code of Iowa and the American Recovery and Investment Act of 2009 (ARRA) for the purpose of providing funds to pay a portion of the costs of constructing improvements and extensions to the water system. If the requirements of ARRA, including, but not limited to, satisfaction of applicable timing requirements are not met and the loan is not forgiven, the Utility will pay interest at 3.0% per annum, an annual .25% servicing fee on the outstanding principal balance (including undisbursed loan proceeds) and an initiation fee of 1% of the authorized loan. The Utility received funds from the DNR upon request to reimburse the Utility for costs as incurred. During the year ended December 31, 2011, the Utility drew down \$560,000 of the forgivable loan, bringing the total drawdowns to the authorized amount of \$560,000. At December 31, 2011, the Utility had not yet met the requirements for the loan to be forgiven.

At December 31, 2011, the Utility had drawn \$10,262,743 including initiation fees of \$140,288.

Expected repayment schedules for all of the Utility's long-term debt are as follows:

Year Ended	<u>Fully Matured</u>		<u>City of Ottumwa</u>		<u>IDNR SRF</u>		<u>Total</u>	
<u>December 31</u>	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>
2012	\$ 7,000	\$ 1,562	\$ 61,530	\$ 23,751	\$ 452,000	\$ 232,132	\$ 520,530	\$ 257,445
2013	-	-	63,530	21,751	526,000	217,462	589,530	239,213
2014	-	-	65,594	19,687	482,743	202,331	548,337	222,018
2015	-	-	67,726	17,555	495,000	187,665	562,726	205,220
2016	-	-	69,927	15,354	509,000	172,605	578,927	187,959
2017 to 2021	-	-	191,802	50,344	2,791,000	620,565	2,982,802	670,909
2022 to 2026	-	-	172,711	23,370	2,708,000	207,870	2,880,711	231,240
2027	-	-	<u>37,983</u>	<u>1,234</u>	-	-	<u>37,983</u>	<u>1,234</u>
	\$ <u>7,000</u>	\$ <u>1,562</u>	\$ <u>730,803</u>	\$ <u>173,046</u>	\$ <u>7,963,743</u>	\$ <u>1,840,630</u>	\$ <u>8,701,546</u>	\$ <u>2,015,238</u>

NOTE 11 – RISK MANAGEMENT

The Utility is exposed to various risks of loss related to torts; theft, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years. The Utility assumes liability for any deductibles and claims in excess of coverage limitations.

OTTUMWA WATER WORKS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011

NOTE 12 – MAJOR CUSTOMERS

Sales to two major customers accounted for greater than 50% of total sales for the year ended December 31, 2011. At December 31, 2011, amounts due from these customers were \$237,775.

NOTE 13 – COMMITMENTS AND CONTINGENCIES

The Utility has signed various contracts for current construction projects in conjunction with the City of Ottumwa, Iowa. Amounts on those contracts will be paid as progress on the projects occurs.

NOTE 14 – OTHER POSTEMPLOYMENT BENEFITS (OPEB)

Plan Description – The Utility operates a single-employer retiree benefit plan which provides medical benefits for retirees and their spouses. There are 5 active and 13 retired members in the plan. The current eligible group is frozen, there will be no new entrants to the plan.

The medical coverage is provided through a partially self funded plan administered by Cottingham Butter.

Funding Policy – The contribution requirements of plan members are established and may be amended by the Utility. The Utility currently finances the retiree benefit plan on a pay-as-you-go basis.

Annual OPEB Cost and Net OPEB Obligation – The Utility's annual OPEB cost is calculated based on the annual required contribution (ARC) of the Utility, an amount actuarially determined in accordance with GASB Statement No. 45. The ARC represents a level of funding which, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed 30 years.

The following table shows the components of the Utility's annual OPEB cost for the year ended December 31, 2011, the amount actually contributed to the plan and changes in the Utility's net OPEB obligation:

Annual required contribution	\$ 79,624
Interest on net OPEB obligation	1,715
Adjustment to annual required contribution	(913)
Annual OPEB cost	80,426
Contributions made	(71,000)
Increase in net OPEB obligation	9,426
Net OPEB obligation beginning of year	42,878
Net OPEB obligation end of year	\$ 52,304

For calculation of the net OPEB obligation, the actuary has set the transition day as January 1, 2009. The end of year net OPEB obligation was calculated by the actuary as the cumulative difference between the actuarially determined funding requirements and the actual contributions for the year ended December 31, 2011.

For the year ended December 31, 2011, the Utility contributed \$71,000 to the medical plan.

The Utility's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan and the net OPEB obligation are summarized as follows:

<u>Year Ended</u> <u>December 31,</u>	<u>Annual</u> <u>OPEB Cost</u>	<u>% of</u> <u>Annual OPEB</u> <u>Cost Contributed</u>	<u>Net</u> <u>OPEB</u> <u>Obligation</u>
2009	\$ 82,809	71.25%	\$ 23,809
2010	80,069	76.18	42,878
2011	80,426	88.83	52,304

OTTUMWA WATER WORKS

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011

NOTE 14 – OTHER POSTEMPLOYMENT BENEFITS (OPEB) (Continued)

Funded Status and Funding Progress – As of January 1, 2009, the most recent actuarial valuation date for the period January 1, 2011 through December 31, 2011, the actuarial accrued liability was \$1,360,045 with no actuarial value of assets, resulting in an unfunded actuarial accrued liability (UAAL) of \$1,360,045. The covered payroll (annual payroll of active employees covered by the plan) was \$284,278 and the ratio of the UAAL to covered payroll was 4.78%. As of December 31, 2011, there were no trust fund assets.

Actuarial Methods and Assumptions – Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumption about future employment, mortality and the health care cost trend. Actuarially determined amounts are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The Schedule of Funding Progress, presented as Required Supplementary Information in the section following the Notes to Financial Statements, will present multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits

Projections of benefits for financial reporting purposes are based on the plan as understood by the employer and the plan members and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

As of the January 1, 2009 actuarial valuation date, the unit credit actuarial cost method was used. The actuarial assumptions includes a 4% discount rate based on the Utility's funding policy. The projected annual medical trend rate is 5%. The ultimate medical trend rate is 4%. The medical trend rate is reduced 0.5% each year until reaching the 4% ultimate trend rate.

Mortality rates are from the RP2000 Mortality Table, applied on a gender-specific basis. Annual retirement and termination probabilities were developed using the alternate valuation method as prescribed in GASB 45.

The UAAL is being amortized as a level percentage over 30 years.

NOTE 15 – SUBSEQUENT EVENTS

Subsequent events have been evaluated through September 25, 2012, the date the financial statements were available to be issued.

REQUIRED SUPPLEMENTARY INFORMATION

OTTUMWA WATER WORKS

BUDGETARY COMPARISON SCHEDULE OF
RECEIPTS, DISBURSEMENTS AND CHANGES IN
BALANCES - BUDGET AND ACTUAL
YEAR ENDED DECEMBER 31, 2011

	<u>Actual</u>	<u>Adjustments</u>	<u>Net</u>	<u>Budget</u>	<u>Variance Favorable (Unfavorable)</u>
Receipts:					
Intergovernmental	\$ 1,125,830	\$ -	\$ 1,125,830	\$ -	\$ 1,125,830
Use of money and property	84,144	-	84,144	105,000	(20,856)
Charges for service	5,806,256	-	5,806,256	5,377,883	428,373
Miscellaneous	-	-	-	36,000	(36,000)
	<u>7,016,230</u>	<u>-</u>	<u>7,016,230</u>	<u>5,518,883</u>	<u>1,497,347</u>
Disbursements:					
Business-type activities	<u>5,707,509</u>	<u>2,639,607</u>	<u>8,347,116</u>	<u>9,021,730</u>	<u>674,614</u>
Excess (deficiency) of receipts over (under) disbursements	1,308,721	(2,639,607)	(1,330,886)	(3,502,847)	2,171,961
Other financing sources, net	-	902,743	902,743	2,400,000	(1,497,257)
Excess (deficiency) of receipts and other financing sources over (under) disbursements	\$ <u>1,308,721</u>	\$ <u>(1,736,864)</u>	\$ <u>(428,143)</u>	\$ <u>(1,102,847)</u>	\$ <u>674,704</u>

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION - BUDGETARY REPORTING

YEAR ENDED DECEMBER 31, 2011

The budgetary comparison is presented as Required Supplementary information in accordance with Government Accounting Standards Board Statement No. 41 for governments with significant budgetary perspective differences.

In accordance with the Code of Iowa, the Utility annually adopts a budget on the modified accrual basis following required public notice and hearing. The budget may be amended during the year utilizing similar statutorily prescribed procedures.

Formal and legal budgetary control is based upon nine major classes of expenses known as functions, not by fund. These nine functions are: public safety, public works, health and social services, culture and recreation, community and economic development, general government; debt service, capital projects and business-type activities. Although the budget document presents function expenses by fund, the legal level of control is at the aggregated function level, not by fund. During the year, there were no budget amendments.

OTTUMWA WATER WORKS

SCHEDULE OF FUNDING PROGRESS FOR THE
RETIREE HEALTH PLAN

REQUIRED SUPPLEMENTARY INFORMATION

<u>Year Ended December 31,</u>	<u>Actuarial Valuation Date</u>	<u>Actuarial Value of Assets (a)</u>	<u>Actuarial Accrued Liability (AAL) (b)</u>	<u>Unfunded AAL (UAAL) (b - a)</u>	<u>Funded Ratio (a/b)</u>	<u>Covered Payroll (c)</u>	<u>UAAL as a Percentage of Covered Payroll ((b-a) / c)</u>
2011	January 1, 2009	\$ -	\$ 1,360,045	\$ 1,360,045	0%	\$ 284,278	4.78%
2010	January 1, 2009	\$ -	\$ 1,360,045	\$ 1,360,045	0%	\$ 288,756	4.71%
2009	January 1, 2009	\$ -	\$ 1,360,045	\$ 1,360,045	0%	\$ 280,849	4.84%

See Note 14 in the accompanying Notes to Financial Statements for the plan description, funding policy, annual OPEB cost, net OPEB obligation, funded status and funding progress.

OTHER SUPPLEMENTARY INFORMATION

OTTUMWA WATER WORKS
DETAIL SCHEDULE OF REVENUES AND EXPENSES
YEAR ENDED DECEMBER 31, 2011

OPERATING REVENUE:

Sale of water	\$ 4,887,878
Sale of electricity	492,983
Miscellaneous income:	
Fire protection - Private	144,775
Customer forfeitures	36,367
Service connections	41,784
Service charge - Sewer billing	52,507
Service charge - Refuse billing	27,719
Miscellaneous	122,243
TOTAL OPERATING REVENUE	<u>5,806,256</u>

OPERATING EXPENSES:

Production:	
Supervision	64,407
Maintenance labor	88,660
Operations labor	207,204
Chemicals/carbon	332,715
Laboratory supplies	14,381
Employee benefits/taxes	237,134
Supplies/maintenance	295,405
	<u>1,239,906</u>

Distribution:

Supervision	62,910
Maintenance labor	253,046
Maintenance materials	114,209
Labor	113,376
Contract street repairs	559,547
Employee benefits/taxes	294,325
Supplies/maintenance	67,545
	<u>1,464,958</u>

Hydro:

Operations labor	81,953
Maintenance supplies	21,740
Lease and rentals	16,159
Contract labor	18,387
Employee benefits/taxes	68,999
Supplies/maintenance	11,074
	<u>218,312</u>

Financial services:

Financial services supervision	50,788
Financial services labor	93,340
Office supplies	8,651
Postage expense	51,138
Customer deposit accounts interest	438
Noncollectible accounts	16,500
Employee benefits/taxes	83,234
Supplies/maintenance	112
	<u>304,201</u>

OTTUMWA WATER WORKS

DETAIL SCHEDULE OF REVENUES AND EXPENSES
YEAR ENDED DECEMBER 31, 2011

OPERATING EXPENSES: (Continued)

Administration:

Executive salaries	79,630
Board salaries	1,825
Vacation pay	50,017
Holiday expense	29,414
Longevity expense	10,703
Casual pay	14,988
Sick pay	15,639
Payroll tax - FICA	104,108
Payroll tax - IPERS	101,850
Training expense	5,031
Subscriptions	1,730
Legal services	24,589
Employee benefits allocated to other departments	(158,945)
Business expense	5,227
Supplies/maintenance	115
	<u>285,921</u>

General plant:

Employee's miscellaneous expense	17,543
General property expense	56,137
Safety program	12,797
Liability insurance	71,355
Workmen's compensation insurance	13,551
Group health insurance	398,737
Group term life insurance	2,490
Health insurance - Retirees	104,718
Contract labor	70,607
Fuel and power	266,230
General services/contingency	93,403
Gas and oil	38,990
Employee benefits allocated to other departments	(402,608)
Supplies/maintenance	16,600
	<u>760,550</u>

Depreciation and amortization 1,143,170

TOTAL OPERATING EXPENSES 5,417,018

OPERATING INCOME 389,238

NONOPERATING REVENUE (EXPENSE):

Grants proceeds	565,830
Forgivable loan proceeds	560,000
Interest income	84,144
Interest expense	(290,491)
Total nonoperating revenue (expense)	<u>919,483</u>

CHANGE IN NET ASSETS \$ 1,308,721

INDEPENDENT AUDITOR'S REPORT ON INTERNAL
CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE
AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

Board of Trustees
Ottumwa Water Works
Ottumwa, Iowa

We have audited the accompanying financial statements of Ottumwa Water Works, as of and for the year ended December 31, 2011, and have issued our report thereon dated September 25, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Ottumwa Water Works' internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Ottumwa Water Works' internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Ottumwa Water Works' internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses therefore, there can be no assurance all deficiencies, significant deficiencies or material weaknesses have been identified.

A deficiency in internal control exists when the design or operation of the control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control such that there is reasonable possibility that a material misstatement of Ottumwa Water Works' financial statements will not be prevented or detected and corrected on a timely basis. We noted no deficiencies in internal control that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Utility's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, non-compliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of non-compliance or other matters required to be reported under Government Auditing Standards.

Comments involving statutory and other legal matters about the Utility's operations for the year ended December 31, 2011 are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the Utility. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes.

Ottumwa Water Works' responses to findings identified in our audit are described in the accompanying Schedule of Findings. While we have expressed our conclusions on the utility's responses we did not audit Ottumwa Water Works' responses and, accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the officials and customers of the Utility and other parties to whom the Utility may report and is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of Ottumwa Water Works during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

ANDERSON, LARKIN & CO. P.C.

Ottumwa, Iowa
September 25, 2012

OTTUMWA WATER WORKS
SCHEDULE OF FINDINGS
YEAR ENDED DECEMBER 31, 2011

Part I: Findings Related to the Financial Statements

INTERNAL CONTROL DEFICIENCIES:

No matters were noted.

INSTANCES OF NON-COMPLIANCE:

No matters were noted.

Part II: Other Findings Related to Required Statutory Reporting

- II-A-11 Certified Budget – Disbursements during the year ended December 31, 2011 did not exceed the amounts budgeted.
- II-B-11 Questionable Expenses – No expenses that we believe may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979 were noted.
- II-C-11 Travel Expense – No expenditures of money for travel expenses of spouses of Utility officials or employees were noted.
- II-D-11 Business Transactions – No business transactions between the Utility and Utility officials or employees were noted.
- II-E-11 Bond Coverage – Surety bond coverage of Utility officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to insure that the coverage is adequate for current operations.
- II-F-11 Trustee Minutes – No transactions were found that we believe should have been approved in the minutes but were not.
- II-G-11 Revenue Bonds – No instances of non-compliance with the revenue bond provisions were noted.
- II-H-11 Deposits and Investments – No instances of noncompliance with the deposit and investment provisions of Chapter 12B and 12C of the Code of Iowa were noted.